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The Federal Budget: What Happened to the Surplus?
By Gary S. Olson, Director

At the close of fiscal year (FY) 1998, the Federal budget recorded a surplus of $69 billion. This marked the first Federal budget surplus since FY 1969. The Federal budget surplus increased to $127 billion in FY 1999 and to $236 billion in FY 2000; the FY 2001 budget closed with a $127 billion surplus. The debate on the Federal budget in Washington, D.C., quickly shifted from a debate centered around eliminating Federal budget deficits to a debate as to the proper action to deal with Federal budget surpluses. As quickly as the Federal budget debate in Washington shifted, the Federal budget surplus disappeared. The Federal budget closed FY 2002 with a $158 billion deficit and it now appears as though the Federal budget deficit will reach $274 billion in FY 2003. This article attempts to explain how the Federal budget went from a $236 billion surplus in FY 2000 to a projected $274 billion deficit in FY 2003. This $510 billion swing in the condition of the Federal budget over a three-fiscal year period is unprecedented in Federal budget history.

Table 1 provides a summary of Federal revenues, expenditures, and surplus/(deficit) for the period FY 1998 through FY 2003, as projected. The FY 2003 expenditure number assumes that the United States Congress approves the President's FY 2003 supplemental appropriation request submitted on March 25, 2003. This supplemental appropriation request provides for $74.7 billion of Federal expenditures for national defense and homeland security issues. The data for FY 1998 through FY 2002 are actual data and the estimates for FY 2003 are current estimates of the nonpartisan Congressional Budget Office.

Table 1
Federal Government Revenues, Expenditures and Year-End Balance (billions of dollars)

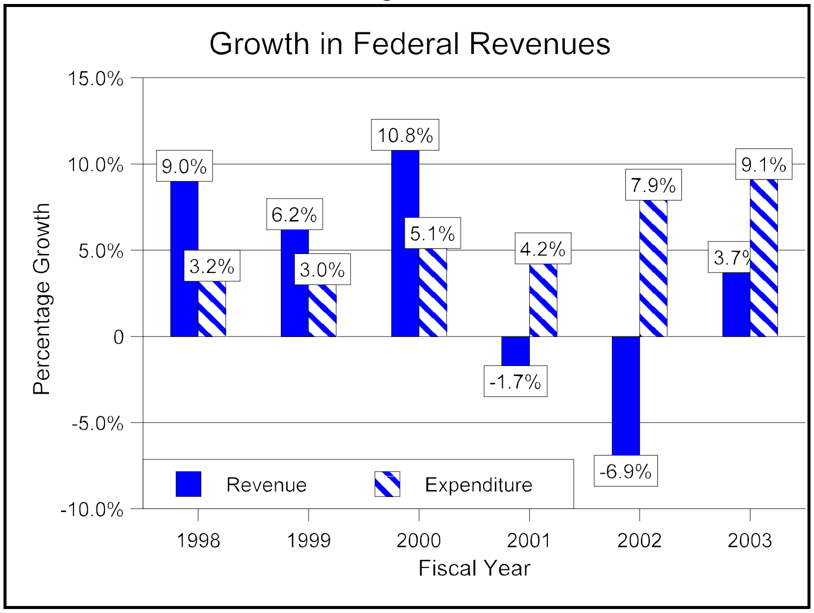
Fiscal Year	Revenues	Expenditures	Surplus/(Deficit)
1998	$1,722	$1,653	$69
1999	1,828	1,701	127
2000	2,025	1,789	236
2001	1,991	1,864	127
2002	1,853	2,011	(158)
2003	1,922	2,196[a)]	(274)

a) Assumes passage of President Bush's FY 2003 supplemental appropriation request of $74.7 billion submitted to Congress on March 25, 2003.

Source: Congressional Budget Office, January 2003.

Figure A provides a graphic summary of the annual percentage change in Federal revenues and expenditures over the same time period. The dramatic change in the overall condition of the Federal budget is largely explained by the data in Figure A. The recent trends in Federal revenue collections and Federal expenditures are the major cause of the recent change in the overall condition of the Federal budget.

Figure 1



Federal revenues, which grew by an average annual rate of 8.1% for the period FY 1993 through FY 2000, have declined during both FY 2001 and FY 2002. This two consecutive fiscal year decline in Federal revenues has happened only rarely in Federal budget history. The last time Federal revenues declined for two consecutive fiscal years was during the FY 1946 and FY 1947 period. Other than this time period, since FY 1900, Federal revenues have declined in at least two consecutive fiscal years only in FY 1931 and FY 1932, and revenues declined for three consecutive fiscal years in FY 1921, FY 1922, and FY 1923. What also marks the recent decline in Federal revenues is the magnitude of the decrease in FY 2002. Federal revenues declined by 6.9% in FY 2002, which marks the steepest annual decline in Federal revenues since FY 1946 when Federal revenues dropped by 14.7%. The decline in Federal revenues that occurred in FY 2002 can be attributed to the recent performance of the United States economy, a significant drop in the realization of capital gains, and the impact of Federal tax policy changes.

Federal expenditures, which grew by an annual average rate of 3.3% for the period FY 1993 through FY 2000, have grown much more significantly in the FY 2001, FY 2002, and FY 2003 period. During FY 2001, Federal expenditures increased by 4.2%. During FY 2002, this rate of expenditure growth accelerated to 7.9%, and the latest projection for Federal expenditure growth in FY 2003 is 9.1%. The projected 9.1% growth in Federal expenditures during FY 2003 represents the largest annual growth in Federal expenditures since FY 1990, when Federal expenditures increased by 9.6%. The growth in Federal expenditures that has occurred over the past three fiscal years can be attributed to large increases in defense spending and substantial increases in other Federal programs such as Medicaid and payments for unemployment benefits.

Table 2 provides more detail regarding the performance of Federal revenues for the FY 1998 through FY 2003 period. The decline in Federal revenues during the FY 2001 and FY 2002 period was fueled by significant decreases in both individual and corporate income tax collections. Individual income tax collections declined by 1.1% in FY 2001 and dropped by a steep 13.7% in FY 2002. Corporate income tax collections declined by 27.0% in FY 2001 and by 2.0% in FY 2002. Individual income tax collections fell as a result of declines in the realization of capital gains, the general state of the economy, and the impact of Federal individual income tax reduction. Corporate income tax collections fell as a result of falling corporate profits, which were affected by the general state of the economy. The performance of individual income tax collections during FY 2001 and FY 2002 marks a sharp contrast from recent years. Individual income tax collections had increased by an annual average of nearly 11.0% in the prior six fiscal years. The other large component of Federal revenues, social insurance taxes, continued to grow throughout the entire period. Social insurance taxes consist of Social Security payroll taxes and Medicare payroll taxes.

Table 2

Recent Trends in Federal Revenues (billions of dollars)

Fiscal Year	Individual Income	Corporate Income	Social Insurance	All Other	Total
1998	$829	$189	$572	$132	$1,722
1999	880	185	612	151	1,828
2000	1,005	207	653	160	2,025
2001	994	151	694	152	1,991
2002	858	148	701	146	1,853
2003	899	156	725	142	1,922

Source: Congressional Budget Office, January 2003

Table 3 provides more detail regarding the performance of Federal expenditures for the FY 1998 through FY 2003 period. The large increases in Federal expenditures in FY 2002 and FY 2003 are driven by several factors. First and foremost, defense expenditures increased by 14.1% in FY 2002 and are expected to increase by at least 26.1% in FY 2003. The Federal government's efforts to combat worldwide terrorism and the current war in Iraq have led to these increases in defense spending. It is possible that defense spending in FY 2003 actually will rise by more than 26.1%, as this increase is based on projections of the cost of the war in Iraq as of late March 2003. Nondefense discretionary spending increased by 12.2% in FY 2002 and by 10.4% in FY 2003. Nondefense discretionary spending funds the general operations of the Federal government and other programs such as transportation, education, economic and workforce development, and health research. Cost increases in mandatory Federal medical programs also have increased in the past two fiscal years. Federal expenditures on the Medicaid program rose by 13.8% in FY 2002 and by 6.1% in FY 2003. Federal expenditures on the Medicare program increased by 6.7% in FY 2002 and 5.9% in FY 2003. Offsetting some of these recent large increases in Federal expenditures has been a significant drop in Federal expenditures on servicing the Federal debt. Interest payments on the Federal debt have declined for the past four fiscal years, including a 17.0% decline in FY 2002 and a 8.2% decline in FY 2003.

Table 3

Recent Trends in Federal Expenditures
(billions of dollars)

Fiscal Year	Defense	Nondefense Discretionary	Medicaid/ Medicare Social Security	Interest	All Other	Total Outlays
1998	$270	$282	$688	$241	$172	$1,653
1999	275	297	704	230	196	1,702
2000	295	320	739	223	212	1,789
2001	306	343	797	206	212	1,864
2002	349	385	855	171	251	2,011
2003[a)]	440	425	900	157	272	2,194

a) Assumes passage of President Bush's FY 2003 supplemental appropriation request of $74.7 billion submitted to Congress on March 25, 2003.

Source: Congressional Budget Office, January 2003

In summary, the Federal budget has undergone a significant transition in recent years. Federal budget deficits in the period FY 1970 through FY 1997 gave way to four consecutive years of Federal budget surpluses beginning in FY 1998. The condition of the Federal budget turned around again in FY 2002 as deficits returned. How long the United States will face Federal budget deficits depends on the future course of the national economy coupled with Federal fiscal policies enacted by the United States Congress and the President. In reviewing the recent condition of the Federal budget one fact is certain: Federal budget conditions can change rapidly.

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Tuition at Michigan's Public Universities
By Ellen Jeffries, Deputy Director

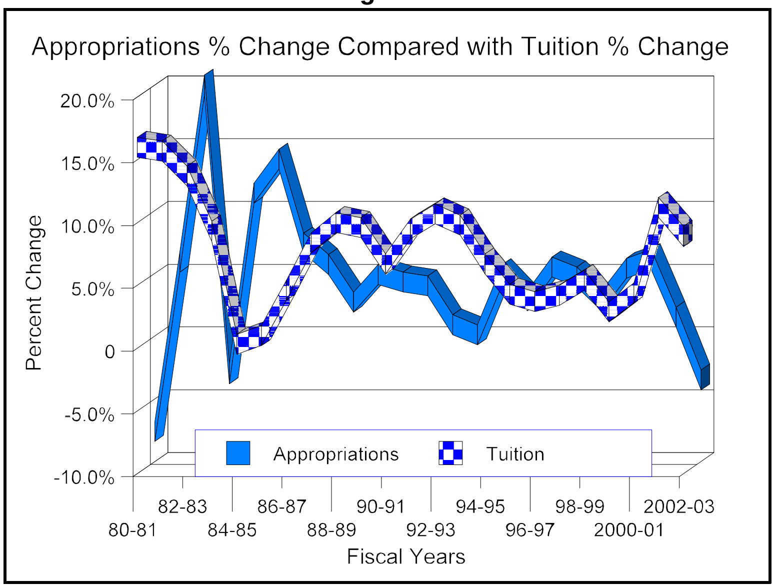
Tuition rates at Michigan's 15 public universities are always the subject of intense discussion during the annual review of Higher Education appropriations. For fiscal year (FY) 2002-03, language was included in the Higher Education appropriations act (Public Act 144 of 2002, Sec. 436) to encourage universities to restrain tuition increases. The language provided that a university's State appropriation would *not* be reduced if that university adopted a tuition and fee rate increase for resident undergraduate students that was 8.5% or less over the prior year, or a total increase of $425 or less over the prior year, whichever was greater. If a university's increase exceeded that limit, the language authorized the State Budget Director to withhold funds appropriated for that university by an amount equal to the amount in excess of the desired tuition restraint. There were three universities that did not initially meet the tuition restraint criteria for academic year 2002-03 but before any action could be taken by the State Budget Director, Executive Order 2002-22 reduced appropriations to universities by 2.5%, essentially neutralizing the tuition restraint agreement.

The Governor's FY 2003-04 budget recommendation for Higher Education does not include the FY 2002-03 tuition restraint language but does state (in Sec. 404): "As a condition to receiving the appropriations in part 1, public universities shall adopt reasonable tuition and fee increases for the 2003-04 academic year." Because the Governor's FY 2003-04 Higher Education appropriation recommendation reduces the Operations line item of each university by 6.74% from its FY 2002-03 year-to-date amount (which includes reductions from both Executive Order 2002-22 and Executive Order 2003-3), it is very likely that all 15 public universities will increase their tuition for the academic year 2003-04.

History of Tuition Increases

As Figure 1 illustrates, when State appropriation increases are low, tuition rate increases tend to be higher to offset the lower appropriations.

Figure 1



In academic year 1991-92, the average for all 15 public universities of annual lower (freshman/sophomore) and upper (junior/senior) division resident tuition and required fees was $2,722; by academic year 2002-03, the average had increased by 98% to $5,388. This compares with a 31.2% increase over that same time period for the Detroit Consumer Price Index, and a 49.5% increase in per-capita personal income. Table 1 lists the annual average undergraduate resident tuition and required fees for academic years 1991-92 through 2001-02, as well as the per-capita personal income for calendar years 1990 through 2002, and calculates the average tuition and fees as a percentage of per-capita personal income. This calculation reveals that in academic year 1991-92, average tuition and fees were 13.4% of per-capita personal income; by 2001-02, tuition and fees had risen to 16.3% of per-capita personal income.

Table 1

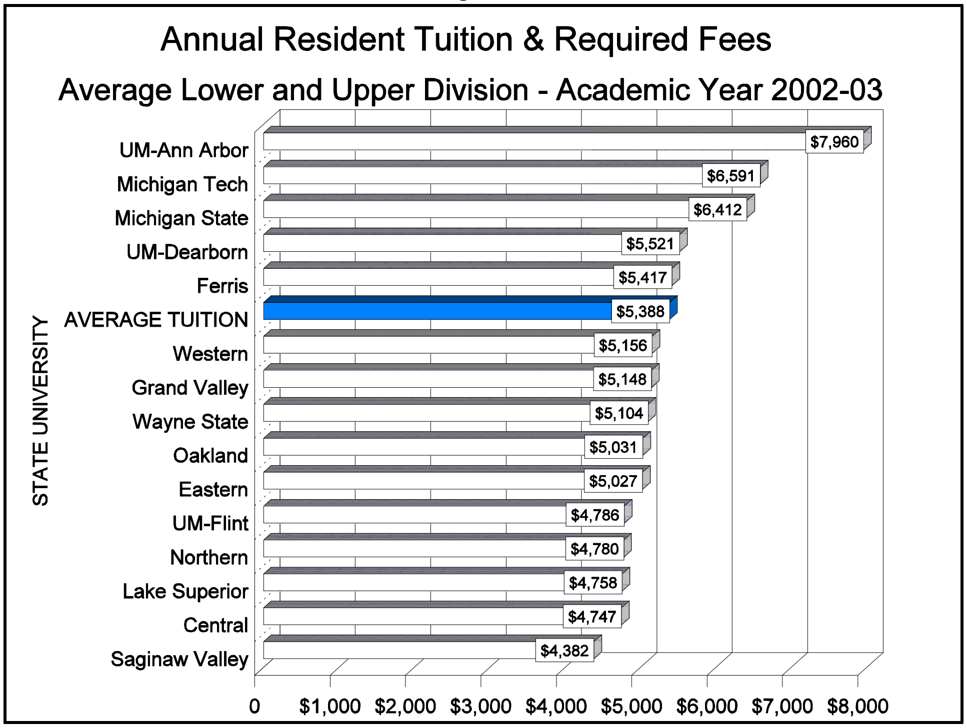
Average Annual Tuition as a Percentage of Per-Capita Personal Income

Academic Year	Average Tuition & Fees	Per-Capita Personal Income	Tuition as a % of Income
1991-92	$2,722	$20,259	13.4%
1992-93	3,014	21,365	14.1
1993-94	3,310	22,830	14.5
1994-95	3,533	23,934	14.8
1995-96	3,686	24,398	15.1
1996-97	3,822	25,509	15.0
1997-98	3,981	26,860	14.8
1998-99	4,196	27,906	15.0
1999-2000	4,260	29,408	14.5
2000-01	4,447	29,629	15.0
2001-02	4,945	30,296	16.3

Academic Year 2002-03

Tuition rates vary among the 15 public universities, and the academic year 2002-03 rates range from an annual average tuition and required fee amount of $4,382 at Saginaw Valley State University to $7,960 at the University of Michigan-Ann Arbor. Figure 2 displays the tuition amounts in descending order and shows an average amount for all 15 public universities of $5,388.

Figure 2



Conclusion

If history is any indication, it is a certainty that 2003-04 tuition and fee rates will increase at all of Michigan's public universities. In public testimony so far during the budget process, university presidents have mentioned potential tuition increases ranging from less than 10% to more than 20%. Depending on what increases there may be in per-capita personal income, the increasing portion of income necessary to finance a higher education raises many policy questions regarding access, affordability, and long-term value, including: Is a higher education being priced beyond the reach of many students and their families? Or, is the investment in a higher education of more value in the long term than other investments are, and therefore worth the price?

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Motorcycle Safety Education and Off-Road Vehicle Safety Programs
By Kathryn Summers-Coty, Fiscal Analyst

The Governor's recommended budget for fiscal year (FY) 2003-04 proposes to eliminate the Motorcycle Safety Education and Off-Road Vehicle (ORV) Safety programs. These programs are currently run by the Michigan Department of Education, and are funded with restricted revenues from vehicle registration and operator license fees. Below are descriptions of both programs, statistics on students served, and a discussion of implications for the future.

Motorcycle Safety Education Program

Before the State issues a motorcycle endorsement on a driver's license, motorcycle safety education is required under the Michigan Vehicle Code (MCL 257.312b) for people less than 18 years of age, or for people 18 or older who have failed a motorcycle driving test twice or more. The safety education courses are subsidized with grants awarded by the Department of Education. These grant dollars are generated by motorcycle operator license fees and motorcycle license plate registration fees.

Annual registration fees for motorcycles are $26, of which $3 is earmarked to the Motorcycle Safety Fund. Original operator endorsement fees are $13.50 and renewals are $5, of which $10 and $3 respectively are earmarked to the Motorcycle Safety Fund. In FY 2001-02, registration fees generated $575,055, and license fees generated $591,260, for combined revenues of $1,166,316 available for grants and administration of the program.

Public instructional providers, such as colleges, universities, intermediate school districts, local school districts, law enforcement agencies, and other governmental agencies, are allowed by law to charge up to $25 in tuition fees to further cover the administration and implementation of the program. (Private providers are not subject to the $25 cap on tuition.) In actual practice, the $25 fee is charged to all students. Table 1 below illustrates the public providers; grant awards and pupils served in 2002; and students served in the last three fiscal years.

Off-Road Vehicle Safety Training

Similar to the motorcycle endorsement requirement, the law requires a person less than 16 years of age, before operating an ORV or All-Terrain Vehicle (ATV), to complete a safety education course approved by the Department of Education (Natural Resources and Environmental Protection Act, MCL 324.81130). Public providers of ORV safety education courses may apply to the Department for grants to subsidize the costs of the program, and also may charge up to $25 (or the cost of one credit hour, in the case of higher educational institutions) for administration and implementation of the course. Private providers are restricted to charging not more than the cost of conducting the course.

The Safety Education Fund is established in MCL 324.81118, and receives $1 from each ORV registration fee of $16.25, renewed on a yearly basis. From this restricted revenue, grants are allocated to public providers. In the 2001-02 fiscal year, $162,037 was generated. Table 2 below illustrates the public and private providers; grant awards and pupils served in 2002; and students served in the last three fiscal years.

Table 1

Motorcycle Safety Program			
Instructional Agency	**Grant Award 2002**	**Pupils Served 2002**	**Total Students Served 2000-2002**
Allegan County Intermediate School District	$108,283	752	1,042
Davenport University	79,778	220	220
Delta College	44,958	386	1,136
Ferris State University	127,663	628	1,653
Flint Public Schools	30,289	183	954
Iosco Regional Educational Service Agency	52,794	141	141
Ithaca Public Schools	10,408	78	200
Lapeer County Sheriff Department	6,935	72	192
Lenawee Intermediate School District	12,338	134	319
Northern Michigan University	74,845	300	872
Otsego County Sheriff Department	49,324	215	621
Schoolcraft Community College	397,893	3,737	10,188
Washtenaw Community College	83,544	847	2,342
White Pigeon Schools	25,193	227	348
TOTAL	**$1,104,243**	**7,920**	**20,657**

Table 2

ORV Safety Program			
Instructional Agency	**Grant Award 2002**	**Pupils Served 2002**	**Total Students Served 2000-2002**
ATV			
Chippewa County Sheriff Department	$12,156	35	77
Clare County Sheriff Department	1,352	10	10
Iosco Regional Educational Service Agency . . .	8,500	60	91
Mecosta County Sheriff Department	1,997	7	40
MATVA (Michigan ATV Association)	34,365	367	510
Wayne County Community College	17,544	72	72
West Iron County Public Schools	16,650	492	1,032
Total	**$92,564**	**1,043**	**1,832**
ORV			
Cycle Conservation Club	$70,705	784	1,836
Ferris State University	3,677	21	114
Luce County Sheriff Department (supplies only)	5,190	0	0
Total	**$79,572**	**805**	**1,950**

For the Future

As mentioned above, the Governor has proposed eliminating both safety programs from the Department of Education's budget beginning in FY 2003-04. According to the *Fiscal Year 2004 Executive Budget* write-up, the elimination is "part of an effort to focus limited state staff resources on core missions ... the department's core focus is providing educational services to children", not providing grants to subsidize safety-training courses for individuals interested in operating motorcycles and off-road vehicles.

The Governor further would eliminate the fees that, to date, have supported these programs, but would retain the safety education requirements. This would have the effect of passing along the full cost of training to individuals seeking operator endorsements for motorcycles and legal use of ORVs, while reducing the registration and license fees. Though individuals would see increased costs initially (due to paying the entire cost of training, rather than $25 as is currently the case), over time, costs to those people would decrease due to the absence of yearly fees for renewals on registrations and licenses.

If the Governor's proposed elimination of the programs occurs, a question remains on the use of fees collected in the current fiscal year that are not spent by September 30, 2003. Would this restricted revenue be transferred into the General Fund, if doing so were allowable? Or, would motorcycle and/or ORV safety grants be provided to the extent of the leftover funds, for limited use in FY 2003-04? At this time, the Department of Education is working with the Department of State to determine their stance on this issue.